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COMMENT

New York Board of Trade

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April 6, 2001

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Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581
Attention: Office of the Secretariat

Re: Regulatory Reinvention

Ladies and Gentlemen:

The Board of Trade of the City of New York Inc. ("NYBOT ®") is pleased to submit these comments on the Commission's proposed rules (the "Proposed Rules") as published in a Federal Register notice (the "Federal Register Notice") on March 9, 2001.

NYBOT welcomes the Commission's efforts to provide guidance with respect to the new provisions of the Commodity Exchange Act (the "Act") as added by the Commodity Futures Modernization Act of 2000 ("CFMA"). It also welcomes the opportunity to participate in the rulemaking through these comments and through discussions with members of the Commission and its staff.

1. On page 14265 of the Federal Register Notice, the Commission requests comments on how and by whom a market-making function may be performed on electronic trading facilities. It would seem that any eligible contract participant ("ECP") who undertakes to maintain a bid and ask spread in accordance with an agreement with, or the rules of, an electronic trading facility should be considered as a functional counterpart to a floor broker or trader and therefore as an "eligible commercial entity," provided that such ECP has adequate capital to meet its obligations as such. See Section 5(d)(11)(A) of the Act. In that connection, we ask that the Commission give clarity to the statutory definition of the term "eligible contract participant" by providing a definition of the term "dealer" as it appears in the Act.

2. On pages 14266 and 14267, the Commission invites public comment on the proposal to permit approval of contracts following certification and to permit a less burdensome certification procedure. This proposal is highly desirable in the interest of promoting operating efficiency, and we strongly endorse it.

3. In paragraph 3 on page 14267, the Commission states that the proposed rules permit but do not require clearing for DTEFs and contract markets. In the case of contract markets, this proposal would appear to run contrary to the Act. Specifically, section 5(b)(5) of the Act states that, as a criterion for designation as a contract market, a board of trade "shall" establish and enforce rules and procedures for insuring the financial integrity of transactions entered into by or through the facilities of the contract market, "including the clearance and settlement of the transactions with a derivatives clearing organization." Section 5(d)(11) establishes as a core principle that a contract market "shall" establish and enforce rules providing for the financial integrity of any contracts traded on the contract market "(including the clearance and settlement of the transactions with a derivatives clearing organization)." By using the word "shall," those two statutory provisions would appear to mandate clearing of contract market transactions through a derivatives clearing organization ("DCO").

4. There are a number of terms used throughout the Proposed Regulations that are not defined anywhere and, in the interest of clarity, should be. These include: "to execute" a transaction, to "effect" a transaction, to "intermediate" transactions, a "participant," a "market participant," a "user" and an "operator" of a contract market.

5. Proposed Section 1.37(c) requires each contract market to keep a record of information regarding any foreign trader "executing" transactions on the exchange. It should be made clear that this only means executing without the interposition of any intermediary.

6. Proposed Section 1.37(d) says that the foreign trader record-keeping requirement shall not apply to a contract market on which transactions are executed through "and" are maintained in accounts carried by registered FCMs. On certain contract markets (including those operated by exchanges owned by NYBOT), orders may be placed directly with floor brokers and not "through" FCMs, although the resulting transactions must be carried by FCMs. Therefore, the word "and" should be changed to "or." The validity of this comment has been recognized in Proposed Section 15.05(h), where the word "or" is used in the same context.

7. Proposed Section 36.2(c)(2) provides that the Commission may render its finding as to whether a facility serves as a significant source for price discovery through the submission of "written" data, views and arguments. The regulation should not preclude oral hearings in appropriate cases. The same applies to the corresponding provision regarding exempt commercial markets in proposed Section 36.3(c)(2).

8. Proposed Section 37.1(b) defines the term "eligible commercial entity" to include a registered floor trader or floor broker whose trading obligations are "guaranteed" by a registered FCM. It is not clear to us why such a guarantee is proposed to be required. If it is a matter of financial integrity, the DTEF should be free to determine for itself what is appropriate. If the Commission is to impose a specified form of credit enhancement, it should be sufficient that a clearing member has agreed to accept all of the trader's or broker's trades, as is currently required on most exchanges.

9. Where a DTEF proposes to trade a product based on a Commission determination, pursuant to Proposed Section 37.3(a)(3)(i), that trading in that product is highly unlikely to be susceptible to the threat of manipulation, we believe it is essential that such DTEF be required to demonstrate that it has had a history of active surveillance to prevent or mitigate market problems. Otherwise, there is a risk that problems in the DTEF's markets could carry over into other markets for the underlying commodity or for the same or similar products traded elsewhere. Therefore, we strongly support the provisions of Proposed Section 37.3(a)(3)(ii)(B)(7). However, the Proposed Section provides that such a determination is to be made after a hearing "through submission of written data, views and arguments." Oral hearings should not be precluded. See paragraph 7, above.

10. Section 37.5 sets forth the procedure for a contract market to operate as a DTEF. Paragraph (a)(2) requires the entity to file a copy of its rules. This should not be necessary, since the rules of the contract market would already be on file with the Commission, unless and to the extent the DTEF rules are different. The same is true as to registration by application in paragraph (b)(3)(i).

11. Section 37.6 regarding compliance with core principles by a DTEF states in paragraph (d) that a DTEF "may" meet the core principles in the manner specified. It should be made clear that the means specified provide safe harbors but are not mandatory.

12. In the proviso to Section 37.7(d), "and" should be "or." See paragraph 6 above.

13. In registration criterion 4, paragraph (b) on page 14275 says that a DTEF allowing customers to qualify as "eligible traders" by trading through an FCM with $20 million of capital should have rules concerning the protection of customer funds that address appropriate minimum financial standards for intermediaries, "the segregation of customer and proprietary funds, the custody of customer funds, the investment standards for customer funds" and other matters. The matters in quotes are and should continue to be subject to Commission regulation. The Act does not provide for requiring DTEFs to have and enforce segregation requirements, and placing such a requirement on DTEFs would impose an

unreasonably onerous burden which even contract markets do not currently bear.

14. In paragraph 1 of Appendix B to Part 37, on page 14275, it is said that the Appendix is "illustrative" only and is not intended to be a mandatory checklist. It omits the sentence that appears in the corresponding provision applicable to contract markets, which is in paragraph 2 of Appendix B to Part 38 on page 14279, stating: "Boards of trade that follow the specific practices outlined under subsection (b) for any core principle in this appendix will meet the applicable core principle." In other words, compliance provides a safe harbor. A similar sentence should be included in Appendix B to Part 37.

15. With respect to core principle 6, Appendix B states on page 14276 that a DTEF must have appropriate fitness standards for certain persons, but then goes on to set forth "minimum standards," which include the bases for refusal to register under Section 8a(2) of the Act and a history of serious disciplinary offenses such as those under Section 1.63 of the Regulations. These minimum standards are not provided for in the statute and would appear to be unnecessarily onerous. Moreover, prescribing what are called "minimum standards" appears to be inconsistent with the statement on page 14265 of the Federal Register Notice that the acceptable practices set forth in the Appendix "are not mandatory in nature." The DTEF should have discretion to determine what are proper grounds for disqualification. Furthermore, this provision provides that natural persons who "directly or indirectly" have greater than a 10% interest in a facility should have to meet the same fitness standards as are applicable to members with voting rights. A natural person who is merely a passive investor and who does not have any official privileges, obligations or responsibilities or otherwise exercise control should not be subject to these standards. Finally, the term "indirectly" is too vague, as is the term "interest." Both should be clarified.

16. Proposed Section 38.2 provides an exemption for various persons, including the "operator" of a contract market. That term appears elsewhere in the Proposed Rules. It is not clear what the term means, and it should be defined.

17. Proposed Section 38.3(b)(4) requires minimum fitness standards for "participants" (which term is not, but should be, defined) having "direct access" to the facility (even though they do not necessarily have voting or any other type of governance rights) and for persons who directly or indirectly have a greater than 10% "ownership interest" (as distinguished from merely an "interest" as in the case of a DTEF), even if they do not have access to the market or do not trade. This seems to go beyond the requirements in Section 5(d)(14) of the Act. Furthermore, the term "direct access" should be clarified. For example, it should not include a customer of an FCM who places an order through that FCM's AORS.

18. Proposed Section 38.4(c) allows a contract market to apply to the Commission for review of its rules solely under Section 15(b) of the Act (taking into account antitrust considerations), without having to seek plenary approval. This is an excellent idea, and we strongly endorse its adoption.

19. In paragraph (a) of designation criterion 5 on page 14279, it is stated that a designated contract market should set appropriate minimum financial standards for "users and/or members." The term "users" is nowhere defined. It should be made clear that this would not require a contract market to establish minimum financial standards for customers of members.

20. Designation criterion 6 on page 14279 says that a contract market must have authority to discipline "market participants." It should be made clear that this would not apply to customers of members.

21. Paragraph (a) under core principle 6 on page 14281 says that a contract market should have procedures and guidelines to carry out emergency decision-making "without" conflicts of interest. That concept is then carried forward two sentences later where it says that the contract market should have procedures and guidelines for notifying the Commission about "preventing" conflicts of interest. However, nothing in the Act requires the contract market to act "without" conflicts of interest or to "prevent" conflicts of interest. Core Principle 11, which is quoted on page 14282, merely says that the contract market must have rules to "minimize" conflicts of interest. Accordingly, the first sentence of paragraph (a) should be changed to read as follows:

    A designated contract market should have clear procedures and guidelines for contract market decision-making regarding emergency intervention in the market, including procedures and guidelines to minimize the effects of conflicts of interests in carrying out [~~carry out~~] such decision-making. [~~without conflicts of interest~~].

    Similarly, in the second sentence thereafter, the word "preventing" should be changed to "minimizing."

22. Paragraph (a) under core principle 7, on page 14281, states that a contract market should have arrangements and resources for the disclosure of contract terms and conditions and trading mechanisms to the Commission, users and the public. A sentence should be added at the end of that paragraph containing substantially the same concept as is set forth in the last sentence of paragraph (a) under core principle 8 on the same page, namely, that such disclosure could be accomplished through means such as timely placement on the contract market's website.

23. Paragraph (a) under core principle 11 on page 14282 would require rules addressing the segregation of customer and proprietary funds, the custody of customer funds, the investment standards for customer funds and related recordkeeping. In view of the fact that all of these factors are and will continue to be subject to regulation by the Commission under Section 4d(2) of the Act, there should be no reason for contract markets to have to adopt additional rules in this area. See paragraph 13, above.

24. Paragraph (b)(1) under core principle 13 on page 14282, requires a designated contract market to provide for dispute resolution mechanisms. Paragraph (b)(5) on the same page provides that a contract market may delegate its responsibility to certain other organizations. The Commission should make explicit that it would be adequate compliance by a contract market if it were simply to adopt rules requiring members to arbitrate claims brought by customers before an organization such as the National Futures Association.

25. Core principle 14 on page 14282 sets forth statutory language requiring a contract market to have fitness standards for certain persons, including "any parties affiliated with" any of those persons. For purposes of this core principle the term "affiliated" with respect to any person should be defined to mean persons controlling or controlled by that person, but should not include persons who are merely under common control with such person or who are linked by some chain of equity ownership not involving control.

26. Proposed Section 40.2 would require a registered DCO to file with the Commission a copy of the rules for any product that it proposes to take on for clearing. That should not be necessary where those rules are already on file, such as where they had been previously submitted to the Commission by the relevant contract market or DTEF.

27. Paragraph (b) of Proposed Section 40.5 states that all rules submitted for approval shall be "deemed" approved if the Commission does not act within the specified period of time. Merely being "deemed" approved may not be sufficient to give the submitting entity the protections to be obtained from actual approval. Accordingly, the regulation should require the Commission affirmatively to approve any such rule within the specified period, unless the Commission affirmatively determines not to do so. The same comment is applicable to paragraph (f).

28. Paragraph (a) of Proposed Section 40.6 states that a contract market or registered DCO may implement a new rule or rule amendment only if certain conditions have been met. It should be made clear that this only applies to rules or rule amendments that are self-certified and not to rules or rule amendments approved or deemed approved by the Commission.

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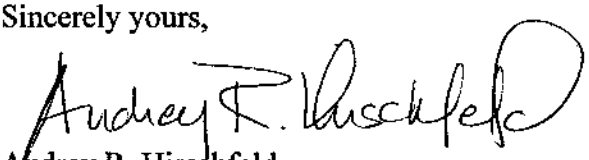
29. In the first sentence of Proposed Section 166.5 (a)(2) on page 14287 some language appears to have been inadvertently dropped out. Presumably the words "is acting," should be inserted after the words "transacting on or through such designated contract market,".

30. Paragraph (c)(5) of Proposed Section 166.5 provides that a registrant must provide customers with a list of organizations whose procedures meet the acceptable practices established by the Commission for dispute resolution. In order for a registrant to comply with that requirement, it would be necessary for the Commission to publish such a list and update it periodically.

31. Paragraph (g) of Proposed Section 166.5 provides that an ECP may agree to resolve any claim or grievance by any settlement procedure. The provision should be extended to include any member of the relevant board of trade, whether or not such member qualifies as an ECP.

If any members of the Commission or its staff have any questions about, or would like to discuss any aspects of, the matters raised in these comments or any other matters relating to the Proposed Rules, please call the undersigned at (212) 742-6040.

Sincerely yours,



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